

January 15, 2003

Donald J. Gelinas
Associate Director
Office of Markets, Tariffs and Rates
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

Re: Docket No. PA02-2-000
Supplemental Response of Sempra Energy Trading Corp.

Dear Mr. Gelinas:

We refer you to the May 22, 2002 response (the "May 22 Response") of Sempra Energy Trading Corp. ("SET"), as supplemented, to your May 8, 2002 data request (the "Data Request") in the above-referenced docket. SET is submitting this supplement on its own behalf, and not on behalf of any SET affiliate.¹

The purpose of this supplement is to clarify SET's May 22 Response in light of the CAISO Department of Market Analysis Report dated October 4, 2002 and titled "Analysis of Trading and Scheduling Strategies Described in Enron Memos" (the "CAISO Report") that was recently made public. The CAISO Report mentions SET in connection with its discussion of the "Enron strategies" colloquially known as "Wheel-out," "Scheduling Energy to Collect Congestion Charges," "Death Star," and "Get Shorty."² For the reasons discussed below, these four references to SET in no way contradict, and indeed are consistent with, SET's statements in the May 22 Response.

"Wheel-out"

Nothing in the CAISO Report suggests that SET engaged in "Wheel Out" as described in the Enron Memoranda or in the Data Request. Item F.1. of the Data Request asked SET to admit or deny whether:

The company engaged in activity described in the Enron memoranda as "Wheel Out" during the period 2000-2001. Knowing

¹ Affiliates of SET were separately listed as respondents to Attachment A to the Data Request.

² The CAISO Report borrows these colorful names from the Enron Memoranda even though the behaviors it describes in some cases differ factually from those in the Enron Memoranda.

that an intertie is completely constrained (*i.e.*, its capacity is set at zero), or that a line is out of service, the company schedules a transmission flow over the facility. The company also knows that the schedule will be cut and it will receive a congestion payment without actually having to send energy over the facility.

As part of its discussion of “Wheel-out,” however, the CAISO Report includes a table purporting to depict counterflow revenues that scheduling coordinators received on out-of-service tie points. (CAISO Report, Table 9 at p. 26.) While SET is identified on the table as a recipient of such revenues, the CAISO Report expressly acknowledges that a market participant, such as SET, could have collected such revenue without knowing that an intertie was out of service:

[N]ot all counterflow schedules on tie lines that are out of service may [be] attributable to intentional gaming, since an SC made [sic] schedule or submit adjustment bids on a line prior to notification of the line outage[.]

(CAISO Report at p. 25 (emphasis added).) Moreover, given the vagaries inherent in the scheduling process, a scheduling coordinator that submitted schedules or adjustment bids *after* receiving notification of an outage from the CAISO would still not have *known* that it would receive a congestion payment without actually sending energy over the facility (or if not sending energy over the facility would be economically desirable given the real-time prices associated with being long or short energy).

Based on SET’s operational experience and the CAISO’s warnings in its systems notices that grid conditions are subject to rapid and sudden change, that its notices are provided purely for “informational purposes,” and that their accuracy cannot be relied upon or assured, SET, on occasion, submitted valid preferred schedules and adjustment bids after receiving notification of constraints on a facility. In such instances, SET would only receive counterflow payments (and not have physical energy flow) if the CAISO adjusted SET’s preferred schedule to show a final schedule with energy flow (which would be possible if another market participant had scheduled to flow energy in the opposite direction), and if the CAISO then cut SET’s schedule in real-time. SET had no way to know in advance whether any of these events, let alone all of them, would come to pass. And even if SET did receive such a counterflow payment, its long or short position resulting from the schedule cut would still settle at the (potentially unfavorable) real-time price. Thus, that SET may have received certain counterflow payments in connection with schedules or adjustment bids on tie points that were out of service, in no way suggests that SET submitted those schedules or bids *knowing* that the schedule would be cut and that it would receive a congestion payment without actually having to send energy over the facility.

“Scheduling Energy to Collect Congestion Charges”

Similarly, nothing in the CAISO Report suggests that SET engaged in “Scheduling Energy to Collect Congestion Charge II” as described in the Enron Memoranda or in the Data Request. Item J.1. of the Data Request asked SET to admit or deny whether:

The company engaged in activity described in the Enron memoranda as “Scheduling Energy to Collect Congestion Charge II” during the period 2000-2001, in which the company: (i) schedules a counterflow even though it does not have any available generation; (ii) in real time, the Cal ISO charges the company for each MW that it was short; and (iii) the company collects a congestion payment associated with the counterflow scheduled. This activity is profitable whenever the congestion payment is greater than the charge associated with the energy that was not delivered.

SET denied having engaged in this activity: “SET did not schedule a counterflow, without having available generation, in order to collect a congestion payment.”

The CAISO Report is consistent with SET’s denial. In fact, according to the CAISO Report, the “strategy” described in the Enron Memoranda was in actuality almost never pursued by *any* market participant:

The specific gaming opportunity identified in the Enron memos (i.e. when congestion charges are higher than the price cap in effect in the real time energy market) has occurred on a very limited basis (only about 50 times) since 1998.³

(CAISO Report at p. 30.)

Nonetheless, the CAISO Report describes a broader set of behaviors that it characterizes as “Scheduling Energy to Collect Congestion Charges.” The discussion of those behaviors includes a table, which references SET, purporting to depict counterflow revenues that scheduling coordinators received from cutting schedules in real-time. (*Id.*, Table 11 at p. 33.) The CAISO Report expressly cautions, however, that a market participant’s receipt of such counterflow revenues does not indicate that it pursued a “gaming strategy.”

It should be noted that not all counterflow schedules cut in real time represent gaming. Wheel through schedules, for instance, may be cancelled if the SC is unable to . . . procure generations [*sic*] and/or transmission to deliver the “import” leg of a wheel through the ISO system. . . . In some cases the ISO may need to curtail an export due to a de-rate on a tie-line occurring after the Hour Ahead congestion management market is ended.

(CAISO Report at pp. 30-31.) The CAISO, moreover, explains that the information kept in its logs “is typically *not* sufficient to determine the precise reason for the cut, and whether the cut could be due to gaming or not.” (*Id.* at p. 31 (emphasis added).)

³ Of course, the Data Request only covers the time period 2000-2001.

SET at all times had valid schedules and intended to flow physical power with purchase or sale commitments. In fact, SET traders had a standing instruction always to flow power. Due, however, to extenuating circumstances beyond SET's control (some of which are identified in the CAISO Report), SET occasionally received congestion payments in connection with a schedule that was cut for legitimate reasons. That does not contradict, and indeed is consistent with, SET's statement in the May 22 Response that it did not intentionally schedule a counterflow, without available generation, in order to receive a congestion payment.

“Death Star”

As with the other “strategies” discussed above, nothing in the CAISO Report suggests that SET engaged in “Death Star” as that activity is described in the Enron Memoranda or the Data Request. Item C.1. of the Data Request asked SET to admit or deny whether:

The company engaged in activity described in the Enron memoranda as “Death Star” during the period 2000-2001, in which the company schedules energy in the opposite direction of congestion (counterflow), but no energy is actually put onto the grid or taken off of the grid. This allows the company to receive congestion payments from the [CA]ISO.

In its May 22 Response SET denied having engaged in this activity: “SET did not schedule energy in the opposite direction of congestion without actually putting energy onto or taking it off of the grid.”

Moreover, SET acknowledged that there were instances in which it may have received congestion payments, but that they were always in connection with valid and enforceable schedules:

The [CA]ISO occasionally paid SET in connection with its operational grid management needs, but at all times SET's schedules were supported by valid and enforceable purchases, sales and transmission.

The CAISO Report's discussion of the activities it characterizes as “Death Star” is consistent with SET's May 22 Response. Yet, the CAISO Report includes a table, that references SET, purporting to depict congestion revenues from counterflows created by import/export schedules. (CAISO Report, Table 2 at p. 11.) The CAISO derived the data contained in the table “by identifying import/export schedules (of equal quantities) by the same SC that generated congestion revenues from counterflows on interties and/or internal paths within the ISO” (Id. at p. 8.) The CAISO acknowledges, however, that such “matching” would include combinations of export/import schedules that have a distinct physical source and sink outside the CAISO control area and schedules that may be “re-circulated” outside the control area. (Id. at p. 8.) The CAISO expressly cautions that it “does not have sufficient information to determine if these schedules represent actual physical sources and sinks that mitigated congestion.” (Id. at p. 11.) As such, SET's inclusion in Table 2 does not contradict SET's prior statements. Moreover, any SET

schedule that included simultaneous “import/export combinations” would have been completely transparent to the CAISO.

“Get Shorty”

With respect to “Get Shorty,” the CAISO Report is also consistent with SET’s May 22 Response. Item E.1. of the Data Request asked SET to admit or deny the following:

The company engaged in activity described in the Enron memoranda as “Get Shorty” during the period 2000-2001, also known as “paper trading” of ancillary services in which it: (i) sells ancillary services in the Day-ahead market; and (ii) the next day, in the real-time market, the company “zeroes out” the ancillary services by canceling the commitment to sell and buying ancillary services in the real-time market to cover its position.

In its May 22 Response SET denied having engaged in the activity described: “SET did not sell ancillary services in the day-ahead market and later cancel its commitment to do so in the real-time market.”

Nothing in the CAISO Report’s discussion of “Get Shorty” contradicts this statement. Indeed, the CAISO Report does not even mention canceling commitments in the real-time market.

Instead, the CAISO Report focuses on conventional commodities market activity: incidents in which market participants may have sold ancillary services in the day-ahead market and “bought back” those services in the hour-ahead market.

SET disclosed in its May 22 Response that it engaged in precisely such market activity:

SET only sold ancillary services in the day-ahead market at the interties where SET was able to meet its commitments. To the extent that SET or the [CA]ISO adjusted schedules due to changed circumstances (*i.e.*, market opportunities, transmission line deratings or generation outages), SET would have had to transact for ancillary services in the hour-ahead market.

Thus, while the question FERC posed addressed real-time, and the answer SET provided correctly denied having engaged in that activity, SET disclosed that it adjusted its schedules in the hour-ahead market based on, among other things, market opportunities.

Moreover, transactions where SET sold in the day-ahead market and “bought back” ancillary services in the hour-ahead market were done on a fully transparent basis and in accordance with the CAISO tariff. The CAISO tariff contained no prohibition of this market activity. To the contrary, it set forth the manner in which such activity would settle. Moreover, as the CAISO Report points out, it is only now that the CAISO is seeking to implement a tariff modification that will eliminate the opportunity by requiring that ancillary services be bought back in the hour-ahead market at the higher of the day-ahead or hour-ahead price. (CAISO Report at p. 20.)

Other “Strategies”

The portions of the CAISO Report that discuss the alleged behaviors referred to as “Fat Boy,” “Export of California Power,” “Non-Firm Export,” “Load Shift,” and “Ricochet” simply make *no* mention of SET. SET notes, however, that with respect to “Fat Boy” in particular, the CAISO Report dispels the notion that such activity had a detrimental effect on the California market. Rather, the CAISO Report states:

. . . any generation that is scheduled against ‘fictitious load’ [also referred to as “overscheduled” or “fake” load] under this strategy is actually delivered, and is therefore fully visible to ISO operators. As a result, during periods of chronic underscheduling of load by the state’s major IOUs, the net effect of overscheduling of load by other participants is to reduce the overall difference between observed loads and generation that the ISO must meet through its formal real time market (or through out-of-market purchases).

(CAISO Report at p. 4.)

Should you have any questions about these matters, please feel free to contact me.

Sincerely,

Michael A. Goldstein
Senior Vice President and General Counsel